WASHINGTON STATE INVESTMENT BOARD

STATE INVESTMENT BOARD
BOARD ADOPTED POLICIES

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EFFECTIVE DATE: 3/20/03

TITLE: Proxy Voting

SUPERSEDES: 12/20/01

BOARD ADOPTION: 3/20/03

APPROVED: Joseph A. Dear

PURPOSE:

This policy provides guidelines for voting proxies of the companies in which the Washington State Investment Board (WSIB) retains a direct equity position. Proxy voting may be performed by staff, contracted to a third-party vendor, delegated to the investment manager or performed as part of the responsibilities of a commingled fund/partnership.

Currently, the WSIB participates in commingled funds in the following equity areas: passive domestic, passive international, active emerging markets and defined contribution options. In these cases, the WSIB does not retain a direct equity position, but holds units in an institutional commingled fund or shares in a mutual fund. The fund is responsible for establishing appropriate guidelines and voting proxies.

Mutual funds are used in some of the defined contribution plans that the WSIB administers. Like commingled funds, mutual funds are responsible for voting the proxies of the securities that they hold in the fund. These proxies are voted according to the guidelines outlined in the mutual fund prospectus. The WSIB votes the proxies of the individual mutual funds themselves. These proxies usually address changes in fund structure and the appointment of directors.

The WSIB does hold direct equity positions in its active developed markets international portfolios. In an effort to maximize timeliness and minimize the cost of translations, the proxy voting of international portfolios is delegated to the investment manager.

POLICY:

The WSIB or its delegates vote all proposals submitted to stockholders in the best interest of the beneficiaries of the trust to which it has a fiduciary duty. In exercising its judgment with respect to voting proxies, the WSIB or its delegates are governed by their primary duty to advance the economic value of the companies whose securities are held within the boundaries of prudent and responsible corporate behavior. If after careful and thoughtful consideration the WSIB or its delegates believe that the position of corporate management could adversely affect the long-term value of the company, the proxy will be voted against management consistent with the policy adopted by the WSIB.

The basic fiduciary requirements under common law are the duty of loyalty and the duty of care. The prudent investor rule, as applied to proxy voting, means that a fiduciary must carefully analyze the implications of proxy proposals. These duties are (1) the fiduciary actually votes the proxies the plan is entitled to vote; (2) that the votes are made after careful study of the issues; and (3) that reasons can be shown why the votes cast were in the best interest of the plan beneficiaries.

Strategic Role

American corporations are the cornerstones of the free enterprise system, and as such must be governed by the principles of accountability and fairness inherent in our democratic system. The shareholders of American corporations are the owners of such corporations and the directors elected by the shareholders are accountable to the shareholders. The WSIB, in turn, is accountable to their fund beneficiaries. This policy is designed to ensure our manager's continually maximize investment return at a prudent level of risk for the exclusive benefit of fund beneficiaries.

Domestic Equity

The WSIB subscribes to the principles and policies adopted by The Council of Institutional Investors (CII). The CII is an organization of large public funds, labor funds, and corporate pension funds which seeks to address investment issues that affect the size or security of plan assets. Its objectives are to encourage member funds, as major shareholders, to take an active role in protecting plan assets and to help members increase return on their investments as part of their fiduciary obligations. It is recognized as a significant voice for institutional shareholder interests. A copy of the CII principles and core policies is attached. (The latest copy is available on the internet at http://www.cii.org.) CII updates this document annually.

International Equity

Proxy voting in international markets differs somewhat from proxy voting in the U.S. markets due to the various country specific laws and regulations. CII principles and core policies form the basis for voting international proxies and the WSIB's international managers have agreed in theory with CII principles and policies. In implementing this philosophy, the WSIB's international managers follow conventions considered best practice internationally which allow for differences in local market conditions.

Original Policy Adopted 6/29/81
Revised 12/15/92
Revised 11/18/93
Revised 2/20/97
Revised 12/18/97
Revised 12/20/01
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The Council of Institutional Investors'
Corporate Governance Policies

The Council expects that corporations will comply with all applicable federal and state laws and regulations and stock exchange listing standards.

The Council believes every company should also have written disclosed governance procedures and policies, an ethics code that applies to all employees and directors, and provisions for its strict enforcement. The Council posts its corporate governance policies on its web site (www.cii.org); it hopes corporate boards will meet or exceed these standards and adopt similarly appropriate additional policies to best protect shareholders' interests.

In general, the Council believes that corporate governance structures and practices should protect and enhance accountability to, and ensure equal financial treatment of, shareholders. An action should not be taken if its purpose is to reduce accountability to shareholders.

The Council also believes shareholders should have meaningful ability to participate in the major fundamental decisions that affect corporate viability, and meaningful opportunities to suggest or nominate director candidates and to suggest processes and criteria for director selection and evaluation.

The Council believes companies should adhere to responsible business practices and practice good corporate citizenship. Promotion, adoption and effective implementation of guidelines for the responsible conduct of business and business relationships are consistent with the fiduciary responsibility of protecting long-term investment interests.

The Council believes good governance practices should be followed by publicly traded companies, private companies and companies in the process of going public. As such, the Council believes that, consistent with their fiduciary obligations to their limited partners, the general members of venture capital, buyout and other private equity funds should use appropriate efforts to encourage companies in which they invest to adopt long-term corporate governance provisions that are consistent with the Council's policies. (Click here for a copy of a letter that investors may consider sending to general partners.)

The Council believes that U.S. companies should not reincorporate offshore because corporate governance structures there are weaker and therefore reduce management accountability to shareholders.

Council policies neither bind members no corporations. They are designed to provide guidelines that the Council has found to be appropriate in most situations.

I. The board of directors

Annual election of directors. All directors should be elected annually (no classified boards).

Independent board. At least two-thirds of the directors should be independent (i.e., their only non-trivial professional, familial or financial connection to the corporation, its chairman, CEO or any other executive officer is their directorship). The company should disclose information necessary for shareholders to determine whether directors qualify as independent, whether or not the disclosure is required by state or federal law. This information should include all financial or business relationships with and payments to directors and their families and all significant payments to companies, non-profits, foundations and other organizations where company directors serve as employees, officers or directors. (See explanatory notes at end.)

All-independent board committees. Companies should have audit, nominating and compensation committees, and all members of these committees should be independent.

The board (not the CEO) should appoint the committee chairs and members. Committees should be able to select their own service providers. Some regularly scheduled committee meetings should be held with only the committee members (and, if appropriate, the committee's independent consultants) present. The process by which committee members and chairs are selected should be disclosed to shareholders.

Board accountability to shareholders

Majority shareholder votes. Boards should take actions recommended in shareholder proposals that receive a majority of votes cast for and against. If shareholder approval is required for the action, the board should submit the proposal to a binding vote at the next shareholder meeting

Interaction with shareholders. Directors should respond to communications from shareholders and should seek shareholder views on important governance, management and performance matters. All directors should attend the annual shareholders' meeting and be available, when requested by the chair, to answer shareholder questions.

Shareholder-director communication. All companies should establish a mechanism by which shareholders with non-trivial concerns could communicate directly with all directors, including independent directors. At a minimum, there should be an open meeting in connection with the company's annual meeting (before or after) in which shareholders could ask questions and communicate their concerns to the independent directors.

Board evaluation. Boards should evaluate themselves and their individual members on a regular basis. Board evaluation should include an assessment of whether the board has the necessary diversity of skills, backgrounds, experiences, ages, races and genders appropriate to the company's ongoing needs. Individual director evaluations should include high standards for in-person attendance at board and committee meetings and disclosure of all absences or conference call substitutions.

Boards should review the performance and qualifications of any director from whom at least 10 percent of the votes cast are withheld.

Absent compelling and stated reasons, directors who attend fewer than 75 percent of board and board-committee meetings for two consecutive years should not be renominated. Companies should disclose individual director attendance figures for board and committee meetings. Disclosure should distinguish between in-person and telephonic attendance. Excused absences should not be categorized as attendance.

'Continuing directors.' Corporations should not adopt so-called "continuing director" provisions (also known as "dead-hand" poison pills) that allow former directors who have left office to take action on behalf of the corporation.

Board size and service. Absent compelling, unusual circumstances, a board should have no fewer than 5 and no more than 15 members (not too small to maintain the needed expertise and independence, and not too large to be efficiently functional). Shareholders should be allowed to vote on any major change in board size.

Companies should establish and publish guidelines specifying on how many other boards their directors may serve. Absent unusual, specified circumstances, directors with full-time jobs should not serve on more than two other boards. Currently serving CEOs should only serve as a director of one other company, and then only if the CEO's own company is in the top half of its peer group. No person should serve on more than five for-profit company boards.

Board operations. Directors should receive training from independent sources on their fiduciary responsibilities and liabilities. Directors have an affirmative obligation to become and remain independently familiar with company operations; they should not rely exclusively on information provided to them by the CEO to do their jobs.

Directors should be provided meaningful information in a timely manner prior to board meetings, and should be allowed reasonable access to management to discuss board issues. Directors should be allowed to place items on board agendas.

The board should hold regularly scheduled executive sessions without the CEO or staff present. The independent directors should also hold regularly scheduled in-person executive sessions without non-independent directors and staff present.

If the CEO is chairman, a contact director should be specified for directors wishing to discuss issues or add agenda items that are not appropriately or best forwarded to the chair/CEO.

The board should approve and maintain a CEO succession plan.

Auditor Independence. As prescribed by law, the audit committee has the responsibility to hire, oversee and, if necessary, fire the company's outside auditor.

The audit committee should seek competitive bids for the external audit engagement no less frequently than every five years.

The company's external auditor should not perform any non-audit services for the company, except those required by statute or regulation to be performed by a company's external auditor, such as attest services.

The proxy statement should also include a copy of the audit committee charter and a statement by the audit committee that it has complied with the duties outlined in the charter.

II. Shareholder Voting Rights

The shareholders' right to vote is inviolate and should not be abridged.

Access to the proxy. Companies should provide access to management proxy materials for a long-term investor or group of long-term investors owning in aggregate at least 5 percent of a company's voting stock to nominate less than a majority of the directors. Eligible investors must have owned the stock for at least three years. Company proxy materials and related mailings should provide equal space and equal treatment of nominations by qualifying investors.

One share, one vote. Each share of common stock should have one vote. Corporations should not have classes of common stock with disparate voting rights. Authorized unissued common shares that have voting rights to be set by the board should not be issued with unequal voting rights without shareholder approval.

Confidential voting. All proxy votes should be confidential, with ballots counted by independent tabulators. Confidentiality should be automatic and permanent and apply to all ballot items. Rules and practices concerning the casting, counting and verifying of shareholder votes should be clearly disclosed.

Voting requirements. A majority vote of common shares outstanding should be sufficient to amend company bylaws or take other action requiring or receiving a shareholder vote. Supermajority votes should not be required.

A majority vote of common shares outstanding should be required to approve:

*Major corporate decisions concerning the sale or pledge of corporate assets that would have a material effect on shareholder value. Such a transaction will automatically be deemed to have a material effect if the value of the assets exceeds 10 percent of the assets of the company and its subsidiaries on a consolidated basis.

*The corporation's acquiring 5 percent or more of its common shares at above-market prices other than by tender offer to all shareholders.

*Poison pills.

*Abridging or limiting the rights of common shares to (i) vote on the election or removal of directors or the timing or length of their term of office, or (ii) make nominations for directors or propose other action to be voted on by shareholders, or (iii) call special meetings of shareholders or take action by written consent or affect the procedure for fixing the record date for such action.

*Severance payments in excess of two times the person's average annual compensation for the previous three years.

*Provisions resulting in the issuance of debt to a degree that would excessively leverage the company and imperil the long-term viability of the corporation.

Broker votes. Broker non-votes and abstentions should be counted only for purposes of a quorum.

Bundled voting. Shareholders should be allowed to vote on unrelated issues separately. Individual voting issues, particularly those amending a company's charter, bylaws or anti-takeover provisions, should not be bundled.

Stock option plans. Shareholder approval should be required for all equity-based compensation plans that include any director or executive officer of the company, and on plans where the number of reserved shares, together with the company's outstanding equity-based awards and shares available for grant, may have a material impact on the capital structure of the company and the ownership interests of its shareholders (generally, 5 percent dilution).

III. Shareholder Meetings

Corporations should make shareholders' expense and convenience primary criteria when selecting the time and location of shareholder meetings.

Appropriate notice of shareholder meetings, including notice concerning any change in meeting date, time, place or shareholder action, should be given to shareholders in a manner and within time frames that will ensure that shareholders have a reasonable opportunity to exercise their franchise.

Polls should remain open at shareholder meetings until all agenda items have been discussed and shareholders have had an opportunity to ask and receive answers to questions concerning them.

Companies should not adjourn a meeting for the purpose of soliciting more votes to enable management to prevail on a voting item. Extending a meeting should only be done for compelling reasons such as vote fraud, problems with the voting process or lack of a quorum.

Companies should hold shareholder meetings by remote communication (so-called electronic or "cyber" meetings) only as a supplement to traditional in-person shareholder meetings, not as a substitute.

As noted previously, all directors should attend the annual shareholders' meeting and be available, when requested by the chair, to answer shareholder questions.

IV. Director and Management Compensation

CEO pay. Annual approval of at least a majority of a corporation's independent directors should be required for the CEO's compensation, including any bonus, severance, equity-based and/or extraordinary payment.

Boards should award CEOs no more than one form of equity-based compensation.

Pay for directors and managers should be indexed to peer or market groups, absent unusual and specified reasons for not doing so. Boards should consider options with forward contracts to align managers' interests with shareholders'.

Change-in-control provisions. Change-in-control provisions in compensation plans and compensation agreements should be "double-triggered," stipulating that compensation is payable only (1) after a control change actually takes place and (2) if a covered executive's job is terminated as a result of the control change.

Director stock ownership. Absent unusual and compelling circumstances, all directors should own company common stock, in addition to any options and unvested shares granted by the company. Directors should own a meaningful position in the company's common stock, appropriate to their personal circumstances.

Directors should be compensated only in cash or stock, with the majority of the compensation in stock.

Option repricing. Unless submitted to shareholders for approval, no "underwater" options should be repriced or replaced, and no discount options should be awarded.

Companies should disclose in the annual proxy statement whether they have rescinded and re-granted options exercised by executive officers during the prior year or if executive officers have hedged (by buying puts and selling calls or employing other risk-minimizing techniques) shares awarded as stock-based incentive or acquired through options granted by the company. Such practices reduce the risk of stock-based incentive compensation awarded to executive officers and should be disclosed to shareholders.

Stock option expensing. Since stock options granted to employees, directors and non-employees are compensation and have a cost, companies should include these costs as an expense on their reported income statements with appropriate valuation assumptions disclosed.

Explanatory notes: The Council's definition of Independent Director

An independent director is someone whose only nontrivial professional, familial or financial connection to the corporation, its chairman, CEO or any other executive officer is his or her directorship.

Members of the Council believe a narrowly drawn definition of "independent" (coupled with a policy specifying that at least two-thirds of board members should meet this standard) is in the corporation's and all shareholders' ongoing financial interest.

Following are the relationships that Council members believe pose the greatest threat to a director's independence.

A director will not generally be considered independent if he or she:

a) is, or in the past five years has been, employed by the corporation or an affiliate in an executive capacity;

b) is, or in the past five years has been, an employee or owner of a firm that is one of the corporation's or its affiliate's paid advisers or consultants (including law firms, accountants, insurance companies and banks).

c) is, or in the past five years has been, employed by a significant customer or supplier;

d) has, or in the past five years has had, a personal services contract with the corporation, its chairman, CEO or other executive officer or any affiliate of the corporation;

e) is, or in the past five years has been, an employee, officer or director of a foundation, university or other non-profit organization that receives significant grants or endowments from the corporation or one of its affiliates;

f) is, or in the past five years has been, a relative of an executive of the corporation or one of its affiliates;

and

g) is, or in the past five years has been, part of an interlocking directorate in which the CEO or other executive officer of the corporation serves on the board of another corporation that employs the director.